

Internal Revenue Service

Number: **200648021**

Release Date: 12/1/2006

Index Number: 2601.04-01, 2501.01-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B04

PLR-147109-05

Date:AUGUST 09, 2006

Re:

LEGEND:

Settlor =

Son =

Grandchild A =

Grandchild B =

Grandchild C =

Great-grandchild A =

Great-grandchild B =

Great-grandchild C =

Spouse =

Trust =

Trust A =

Trust A-1 =

Trust A-2 =

Trust B =

Trust C =

Trustee A =

Trustee B =

Court =

State =

State Statute =

Date 1 =

Date 2 =

Date 3 =

:

This responds to a letter from your authorized representative dated September 9, 2005, requesting rulings concerning the generation-skipping transfer (GST) tax consequences of a proposed modification of a trust.

FACTS

Settlor created Trust on Date 1, prior to September 25, 1985. Under the Trust instrument three separate trusts were established, one for each of Settlor's granddaughters: Trust A for Grandchild A, Trust B for Grandchild B, and Trust C for Grandchild C. On Date 2, pursuant to applicable State law, State Statute, Trust A for the benefit of Grandchild A was divided into two identical trusts, Trust A-1 and Trust A-2 that continued to be administered according to the terms of Trust prior to the division. The division of Trust A was approved by Court. Grandchild A is married to Spouse and has three children, Great-grandchild A, Great-grandchild B, and Great-grandchild C. Neither Grandchild B nor Grandchild C has or has ever had descendants.

Settlor's child, Son, and Trustee A are the trustees of Trust A-1, Son and Spouse are trustees of Trust A-2, Son and Trustee A are trustees of Trust B, and Son and Trustee B are trustees of Trust C.

Paragraph III.A of Trust provides that the trustees of each separate trust shall distribute to or for the benefit of Grandchild A, Grandchild B, or Grandchild C, respectively, during her lifetime so much of the income and corpus from such trust as the trustees, in their sole discretion, consider necessary or advisable.

Paragraph III.B provides that, upon the death of the respective Grandchild A, Grandchild B or Grandchild C, the trust created for the benefit of the grandchild shall terminate and the remaining corpus and undistributed income is to be distributed to the grandchild's living descendants equally per stirpes, or if none, then in equal shares to the grandchild's surviving sisters or to the living descendants of any deceased sister per stirpes, provided, that any portion distributable to a beneficiary for whom any property is being held in trust under the Trust instrument is to be added thereto. If any portion is to become distributable to a minor, such portion is to immediately vest in such minor, but the trustees are to retain possession until such minor becomes 21 years of age.

The parties propose to modify Paragraph III.B to provide as follows:

Upon the death of the beneficiary of each trust, the trust of such beneficiary shall terminate and the remaining corpus or undistributed income thereof shall be forthwith distributed to her living descendants equally per stirpes, or, if none, then in equal

shares to her surviving sisters or to the living descendants of any deceased sister per stirpes; provided, however, that (i) any portion distributable to any of [Grandchild A, Grandchild B, or Grandchild C] for whom any property is being held in trust hereunder shall be added thereto, and (ii) any portion distributable to a descendant of [Grandchild A, Grandchild B, or Grandchild C] shall immediately vest in such descendant but shall be held, administered and distributed in a Continuation Trust for the benefit of such descendant (or added to such trust, if one is already in existence) described in succeeding Paragraph IIIa. hereof.

In addition, a new paragraph, Paragraph IIIa, will be added to Trust as follows:

A. Designation. To the extent that other provisions of this Agreement shall direct that properties allocable to a descendant of [Grandchild A, Grandchild B, or Grandchild C] shall be held in or added to a Continuation Trust, each such trust shall exist for the primary benefit of that descendant (the "Beneficiary") and be designated by the name of the Beneficiary followed by "Continuation Trust." Each such trust shall be distributed as provided in this Paragraph.

B. Income and Principal. The Trustee shall be authorized to distribute to the Beneficiary so much, or all, of the net income, principal or both of the trust as the Trustee considers advisable for any purpose or purposes whatever, including without limitation to allow the Beneficiary the opportunity to make gifts (tax motivated or otherwise) to charitable organizations or members of the Beneficiary's family. Without intending to limit or expand the discretion granted to the Trustee by the preceding sentence, it is intended that the Trustee be liberal in the exercise of its discretion with respect to distributions to the Beneficiary. Undistributed income, if any, shall be incorporated into the principal of the trust annually.

C. Power of Appointment. If the Beneficiary of a Continuation Trust is a descendant of [Grandchild A], and if [Spouse] survives [Grandchild A], then, following the death of [Grandchild A, Spouse] shall have the continuing discretionary power, exercisable in his individual capacity and not as a fiduciary, by deed to appoint to such Beneficiary, either immediately or thereafter upon a date or dates specified therein and occurring before the termination of such Continuation Trust pursuant to

succeeding subparagraph D, all or any part of the income, principal or both of the trust as [Spouse] in his absolute discretion shall direct. Any exercise of such power directing that distributions to the Beneficiary be made at a date or dates occurring thereafter shall be revocable, in whole or part, before the occurrence of such date or dates by a subsequent deed unless [Spouse] specifically provides otherwise in the original deed. Each such exercise or revocation of a prior exercise of said power shall be accomplished immediately upon delivery to the trustee by [Spouse] of a written instrument of exercise or revocation that is dated, signed and acknowledged by [Spouse]. Notwithstanding the foregoing, [Grandchild A], by duly probated last will and testament or codicil thereto, may cancel, reduce or restrict such power in any respect as to all or any of her descendants.

D. Termination and Distribution. If not earlier terminated through distributions pursuant to preceding subparagraphs B and C, each Continuation Trust shall terminate upon the death of its Beneficiary, or, if earlier, upon a date or dates specified by (i) [Grandchild A], in the case of a descendant of [Grandchild A], (ii) [Grandchild B], in the case of a descendant of [Grandchild B], or (iii) [Grandchild C], in the case of a descendant of [Grandchild C], in her duly probated last will and testament or codicil thereto (i.e., either all at once on a particular date or time or, in whole or in part, in any amounts or proportions, on any two or more dates or times specified in any such will or codicil); provided, that, unless [Grandchild A] shall direct otherwise pursuant to an exercise of her power described in the final sentence of preceding subparagraph C, an exercise by [Spouse] of powers described in the opening sentence of said subparagraph C shall, to the extent inconsistent with the terms of any such will or codicil of [Grandchild A], supersede such terms. Upon termination, the remaining principal and undistributed income of each such trust shall be distributed to the personal representative of the Beneficiary's estate, as such term is defined in the [State] Probate Code, or, should the Beneficiary still be living, to the Beneficiary.

On Date 3, Court issued an order modifying Trust, as described above. The court order is contingent on receipt of a favorable private letter ruling from the Internal Revenue Service.

You have requested a ruling that the proposed modifications of the trust agreement as described above will not cause the trusts to lose its exempt status under § 1433(b)(2)(A) of the Tax Reform Act of 1986 (Act).

Law and Analysis

Section 2601 of the Internal Revenue Code imposes a tax on each generation-skipping transfer. Under § 1433(b)(2)(A) of the Act and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the GST tax does not apply to any generation-skipping transfer under a trust that was irrevocable on September 25, 1985.

Section 26.2601-1(b)(1)(ii)(A) provides that any trust in existence on September 25, 1985, will be considered an irrevocable trust except as provided in § 26.2601-1(b)(1)(ii)(B) or (C) (relating to property includible in the grantor's gross estate under §§ 2038 and 2042).

Section 26.2601-1(b)(4)(i) provides rules for determining when a modification, judicial construction, settlement agreement, or trustee action with respect to a trust that is exempt from the GST tax will not cause the trust to lose its exempt status. The rules contained in the paragraph are generally applicable only for purposes of determining whether an exempt trust retains its exempt status for GST tax purposes. Unless specifically provided otherwise, the rules do not apply in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(D) provides that a modification of the governing instrument of an exempt trust (including a trustee distribution, settlement, or construction that does not satisfy paragraph (b)(4)(i)(A), (B), or (C) of this section) by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13, if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust.

In this case, Trust was irrevocable on September 25, 1985, and there have been no actual or constructive additions to Trust after September 25, 1985. As discussed above, under the proposed modification and court order, the assets in each Continuation Trust immediately vest in the named beneficiary and each Continuation Trust will be held for the exclusive benefit of the named beneficiary during the beneficiary's lifetime. In addition, if not earlier terminated through distributions to the named beneficiary, on the death of the named beneficiary, any remaining principal and undistributed income will be distributed to the personal representative of the beneficiary's estate, and therefore, will be includible in the beneficiary's gross estate for federal estate tax purposes.

Under these circumstances, based on the facts submitted and the representations made, we conclude that the proposed modifications will not shift a beneficial interest in Trust to a beneficiary who occupies a lower generation than the person who held beneficial interests prior to the modification. In addition, the modification will not extend the time for vesting of any beneficial interests beyond the period provided in Trust. Therefore, based on the facts submitted and representations made, we conclude that the proposed modifications will not cause Trust, Trust A-1, Trust A-2, Trust B, or Trust C, to lose exempt status for GST tax purposes.

Except as specifically ruled herein, we express no opinion on the federal tax consequences of the transaction under the cited provisions or under any other provisions of the Code.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the materials submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Pursuant to a power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely yours,

George Masnik
Branch Chief, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure
Copy for section 6110 purposes